Nos. 16042 and 16223
Consolidated cases

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

IRVING I. BASS, Trustee in Bankruptcy of the Estate of ZIPCO, INC., a corporation, Bankrupt,

Appellant,

vs.

ALTMAN FACTORS CO., FRUEHAUF TRAILER CO., and COMAIR PRODUCTS, INC.,

Appellees.

APPELLANT'S OPENING BRIEF.

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TOPICAL INDEX

TABLE OF AUTHORITIES CITED

Cases

Statutes

Textbooks

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IRVING I. BASS, Trustee in Bankruptcy of the Estate of ZIPCO, INC., a corporation, Bankrupt,

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Appellees.

APPELLANT'S OPENING BRIEF.

Statement of Jurisdiction.

The consolidated appeals were consolidated by a Stipulation dated October 22, 1958 and an Order of Consolidation dated November 4, 1958, the Stipulation and Order being set forth at pages 15 to 18 in the Transcript of the Record. The appeal in case No. 16042 is an appeal from an Order of the District Court, Southern District of California, Central Division, dated March 28, 1958 and entered on March 31, 1958, reversing on review Findings of Fact, Conclusions of Law and Order of a Referee in Bankruptcy. Case No. 16228 is an appeal from an Order of the District Court, Southern District of California, Central Division, made and entered on September 23, 1958, and affirming on review Findings of Fact, Conclusions of Law and Order of a Referee in Bankruptcy.

Jurisdiction of the District Court, in each case, existed under Section 2-a(7) of the Bankruptcy Act, United States Code, Title 11, Chapter 2, Section 11, and Jurisdiction of this United States Court of Appeals lies under Section 47(a) and (b) of Title 11, U. S. C. A.

Statement of Case.

These two consolidated appeals involve the identical facts, and the identical issues of law, and each arises out of the identical proceedings. Prior to bankruptcy, the bankrupt corporation received work orders or invoices from various persons or parties, including the Fruehauf Trailer Co. and Com-Air Products, Inc., for precision bushings, which the bankrupt manufactured. These work orders or invoices were accepted by the bankrupt corporation, and in each case contained a prohibition against the assignment of the right to perform the said contracts, and the right to receive payment thereunder. The precise language of these work orders or invoices will be hereinafter set forth in the argument section of this Brief. Subsequently, and in violation of the specific prohibition contained in the work orders and/or invoices, the bankrupt corporation assigned the accounts receivable arising by virtue of performance, to the Appellee, Aetna Factors Co. The Appellee had full knowledge of the prohibitions contained in the contracts, and served no notice upon the obligor companies, Fruehauf Trailer Co. and Com-Air Products, Inc. On the contrary, the Appellee had the bankrupt corporation from time to time collect the assigned accounts and then pay over to the Appellee the moneys so received.

At the time of bankruptcy each of the obligor corporations held funds in their hands, which the Trustee in Bankruptcy demanded of them. Fruehauf Trailer Co. paid

over to the Trustee the Funds in its hands, and Com-Air Products, Inc., held the funds in its hands subject to a determination by the Court concerning the legal ownership thereof. The Appellee made demand upon Fruehauf Trailer Co. and Com-Air Products, Inc., for payment, and in each instance the demands were refused and the said obligors refused to pay, basing their refusals upon the prohibition against assignments contained in their contracts with the bankrupt corporation. The Appellee then filed suit as against Aetna Factors Co. and Fruehauf Trailer Co. in the Superior Court of the State of California, in and for the County of Los Angeles, and the Trustee instituted these proceedings before the Referee.

At each of the hearings in the within matter, Com-Air Products, Inc., and Fruehauf Trailer Co., appeared and actively asserted their rights by and under their contracts, relating to the prohibition against assignment of accounts receivable, and while they appear as Appellees in case No. 16042, they are actually Appellants, as they oppose the payment of any moneys to Aetna Factors Co.

At the conclusion of the various proceedings before the Referee, the Referee made and entered Findings of Fact, Conclusions of Law and an Order to the effect that Aetna Factors Co. had no lien, claim or charge as against the moneys owed by Fruehauf Trailer Co. and Com-Air Products, Inc., and that the said funds should be paid over to the Trustee, finding as a matter of law and under California law, the prohibitions in the various contracts against assignments of the said contracts were valid and enforceable and that the Trustee in Bankruptcy had succeeded to the rights thereunder as a so-called "ideal creditor." The Appellee herein, Aetna Factors Co.. filed a Petition for Review to the United States District Court, and the Honorable William C. Mathes, United States

District Court Judge, after argument, made and entered an Order reversing the Referee in Bankruptcy, and remanding the matter for further proceedings, and further Findings of Fact and Conclusions of Law in accordance with his Order remanding the proceedings. The first of these two appeals was taken from the Order reversing and remanding the matter to the Referee in Bankruptcy. A remanded hearing was held before the Referee, and in accordance with the Order of the District Court, the Referee in Bankruptcy made and entered Findings of Fact, Conclusions of Law and an Order reversing himself. The Trustee, the Appellant herein, then filed a Petition for Review to the United States District Court, and on a hearing Judge Mathes then affirmed the new Findings of Fact, Conclusions of Law and Order. This resulted in the second of these two consolidated appeals.

Specification of Errors Relied Upon.

I.

In connection with case No. 16042, the Court erred in each of the following particulars:

1. Erred in ordering that the Referee's Order of December 23, 1957, and the Findings of Fact and Conclusions of Law made in support thereof, be set aside;

2. Erred in paragraph II of the "Order on Review of the Referee's Order of December 23, 1957," in finding and ruling as a matter of law "inasmuch as the provisions in the subcontracts prohibiting assignments were solely for the benefit of the obligors, the assignments were valid under California law as against the bankrupt assignor and the factor assignee";

3. Erred in not affirming and adopting each and every of the Referee's Findings of Fact and Conclusions of Law of December 23, 1957;

4. Erred in not affirming the Referee's Order of December 23, 1957, and in not dismissing the Petition for Review;

5. Erred in recommitting the matter to the Referee with directions to hold a further hearing;

6. Erred in recommitting the matter to the Referee with directions to make Findings of Fact and Conclusions of Law as to whether or not any of the transactions involved were carried on with intent to hinder, delay or defraud creditors, etc., and in ordering the Referee to enter an appropriate Order or Orders based upon the said Findings of Fact and Conclusions of Law.

II.

Erred in the following particulars relating to Appeal No. 16228:

1. Erred in affirming the Referee's Order of August 25, 1958 in that

2. Conclusion of Law No. IV of the said Order of April 25, 1957 is contrary to law and fact;

3. Conclusion of Law No. V of said Order is contrary to law;

4. Conclusion of Law No. VI is contrary to law;

5. Conclusion of Law No. IX is contrary to law;

6. The Order based upon said Conclusion is contrary to law in paragraphs I, II and III as the same is supported by erroneous Conclusions of Law;

7. In not reversing the Referee's Order of April 25, 1958 and in not finding that as a matter of law the Conclusions of Law in the Referee's Order of December 23, 1957 were correct, and that an Order in conformity therewith should be made and entered.

Summary of Argument.

The Memorandum Opinion of Joseph J. Rifkind, dated May 10, 1957, and found at pages 15 to 22 of the Transcript of the Record, clearly and succinctly summarizes the Trustee's entire argument in this case, and the cases to be cited by the Appellant in the following argument. The Supplemental Memorandum Opinion of the Referee, dated October 15, 1957, and found at pages 24 to 34 of the Transcript of the Record, supplements the aforementioned Memorandum Opinion and is a learned dissertation on the law involved in this Appeal.

The Appellant will argue that there never was any question as to the facts in this case and the only question presented to the Court is purely and simply a question of law. This is demonstrated at page 75 of the Transcript in the paragraph containing bracketed [6]. At page 78 of the Transcript of the Record, Mr. Treister, the attorney for the Appellee, admits that even the Appellee agrees with the Court's decision on summary jurisdiction. At page 78, in the fifth full paragraph, Mr. Treister agrees with the Court that the validity of the prohibition against assignment in the Purchase Orders is a matter to be determined by State law, as stated in page 4 of the Court's Opinion. At page 81 of the Transcript of the Record, in the third full paragraph, Mr. Treister states: "We want to prevail on the real issue in controversy here, namely, whether or not a nonassignability clause in a Purchase Order is valid and enforceable when the Assignor goes into bankruptcy." At page 82 of the Transcript, in the first full paragraph, the Referee points out the difference in the clauses contained in the two contracts and that he commented on it in his Opinion. At page 15 of the Transcript, in the Referee's Memorandum Opinion, the Court

specifically points out and quotes first, the Purchase Order from Fruehauf Trailer Co. and secondly, the nonassignability clause in the Com-Air Products, Inc. No quarrel exists as between the Appellant and the Appellee as to these facts or any other facts as heretofore referred to in the Appellant's Statement of the Case.

The Appellant's whole argument will be that Judge Mathes erred in reversing the Referee and in requiring the Referee to hold as a matter of law (California State Law) the Appellee and Assignee who received an assignment contrary to specific provisions in a Purchase Order, could prevail as against the Trustee in Bankruptcy of the Assignor of the obligation. It will be argued that Section 70-c of the Bankruptcy Act and cases following the same, including *Constance v. Harvey* (C. C. A. 2d), 215 F. 2d 571, 575, Cert. den., 348 U. S. 913; *United States v. Eiland* (C. C. A. 4th), 223 F. 2d 118; *Sampsell v. Straub* (C. C. A. 9th), 194 F. 2d 228 at p. 231; and *England v. Sanderson* (C. C. A. 9th), 236 F. 2d 641 at p. 643, give to the trustee most extensive rights. It will be further argued that the case of *Parkinson v. Caldwell* (1954), 126 Cal. App. 2d 548, petition for hearing denied by the California Supreme Court and the *Allhusen v. Caristo Const. Co.* (N. Y.), 103 N. E. 2d 891, cited by the *Parkinson* case, control the California law in this matter. It will further be argued that these cases hold that the assignee cannot recover where an assignment of a chose in action or of personalty has been made in violation of specific language contained in the contract and that these cases stand for the proposition that a successor in interest of the assignor in this situation would prevail over the assignee.

ARGUMENT.

I.

There Is No Controversy as to the Facts in This Matter.

See the argument set out in the Summary of Argument and see the Transcript of the hearing on the Motion to Reconsider which is set forth at pages 70 to 100 of the Transcript of the Record wherein counsel for the Appellee at numerous places states that the only issue before the Court is a question of law as to the law of the State of California and how the same applies to the facts of this case.

II.

The Purchase Orders of Fruehauf Trailer Co. and of Com-Air Products, Inc. Clearly and Precisely Prohibited Any Assignment of Either the Right to Perform or the Right to Receive Benefits Under the Said Purchase Orders.

As set out in the Referee's Memorandum Opinion, commencing at the bottom of page 15 of the Transcript of the Record on Appeal, the Purchase Order from Fruehauf Trailer Co. to the Appellant's Bankrupt Corporation provides in paragraph V thereof:

> "Assignment. The contract resulting from the acceptance of this Order, or any interest thereunder, shall not be assignable nor shall any part of the work be subcontracted by the Vendor without prior written consent of the purchaser."

The Purchase Order from Com-Air Products, Inc., to the Appellant's Bankrupt, provides in paragraph 15 thereof

> "Assignment and subcontracting. This Order may not be assigned or subcontracted in whole or in any part,

nor may any assignment of any of the money due or to become due hereunder be made by the Vendor without the prior written consent of a buyer in each instance."

This may be found on page 16 of the Transcript of Record.

The Com-Air Products, Inc., prohibition specifically by its language prohibits the assignment of any money due or to become due under the Purchase Order. The language in the Fruehauf Trailer Co. prohibition, "the contract resulting from the acceptance of this Order or any interest thereunder," and specifically the words "or any interest thereunder" would be meaningless if they did not relate to the right to receive moneys as well as to the right to assign the contract. This is illustrated by the fact that the prohibition goes on to prohibit the assignment or the subcontracting of a work by the Vendor. It is submitted that the words "or any interest thereunder" would be meaningless unless they specifically related to money as the only method whereby a portion of a contract and specifically the performance of the contract, could be assigned, would be by subcontracting a portion of the performance of the contract and this is specifically forbidden by the latter portions of the prohibition.

III.

That California State Law and Section 70-c of the Bankruptcy Act Control, Is Clear.

At page 78, in the seventh paragraph of the Transcript of the Record, the attorney for the Appellee admits that as between the parties State law will govern and in the next paragraph above that, on the same page, again admits that the matter is to be determined by State law. On page 79 of the Transcript of the Record, in the third and

fourth full paragraphs on that page, Mr. Treister, the attorney for the Appellee, again admits that we must look to the State law and

> "we are in agreement with the Court's next holding, namely, that we agree that the Court correctly interprets the Trustee lien creditor status on the date of bankruptcy on page 5 of the Opinion.
>
> "At this point I think this may be superfluous but I think this is the only provision under which the Trustee can prevail under Section 70-c of the Bankruptcy Act. . . ."

The cases of *Constance v. Harvey, United States v. Eiland, Sampsell v. Straub, and England v. Sanderson,* all illustrate that the Bankruptcy Act overrides the State law, and *Arnold v. Phillips* (5th Cir.), 117 F. 2d 497 at pp. 500-501, holds:

> ". . . Whether when bankruptcy supervenes a title acquired by one creditor is good as against other creditors, and what are the relative rights and standing of creditors as against each other, and what the propriety of recognizing and enforcing secured debts under varying circumstances, are questions so related to the bankruptcy power as to be regulable by Congress; they are of the essence of bankruptcy law. There necessarily arises also a body of judicial interpretation having the effect of law, which overrides the interpretation of the State courts on similar question. The 'equity' administered in the bankruptcy courts may not be exactly that of the State courts."

IV.

The California State Law Is to the Effect That as Against an Assignee Who Has Received an Assignment of a Chose in Action, in Violation of Prohibitions in the Contract, a Successor of the Assignor May Recover, as Such an Assignment Is Void.

Counsel for the Appellant has exhaustively researched the case reports of the State of California and the most recent case they have been able to discover relating to assignments of choses in action contrary to an express prohibition contained in the contract giving rise to the right, is the case of *Parkinson v. Caldwell,* a 1954 District Court case, reported at 126 Cal. App. 2d 548, 272 P. 2d 934. This was an appeal from a judgment in favor of a plaintiff administrator of the Estate of T. W. Caldwell, in which the plaintiff was decreed to be entitled to the proceeds of a promissory note secured by a Deed of Trust. The facts of this case are somewhat complex and in essence were as follows: As a result of a Will contest, uncle and nephew entered into a compromise which in part provided that the uncle had a claim to be secured by a promissory note and a Deed of Trust in the amount of $13,942.05. The compromise further provided "said note shall be payable to the party of the first part and shall be held by him until it shall become due according to its terms unless there be an agreement between the parties to the contrary. . . ." The note was executed to the uncle and on its face contained the above quoted language: A short time later the uncle executed a promissory note to other parties and as collateral security pledged the promissory note containing the above-cited prohibitory language; on the death of the uncle the nephew deposited the face amount of the note the uncle had been holding,

with a Title Insurance Company and asked the Title Insurance Company to reconvey the note to him; later and prior to the death of uncle, Viola Lester, the surviving joint tenant of the owners of the promissory note of the uncle, demanded that the Title Company pay her the $12,000.00 represented by her note out of the moneys deposited by the nephew on the ground that she held the note and trust deed as security for the uncle's death; Plaintiff, the administrator of the uncle's estate, brought an action praying that he be decreed owner of the original promissory note and of the moneys deposited by the nephew with the Title Company; the trial court found for the plaintiff, that the purported pledge of the note to the uncle and deed of trust to the Lesters was of no force and effect as the same violated the prohibition against assignment contained in the original agreement and on the face of the note. In short, the plaintiff was the successor in interest of the uncle who had violated the language contained in the note and had, contrary to the provisions of the note, assigned the same by pledging it to secure a trust deed, and a successor in interest of the uncle was allowed to prevail over the one to whom the same was pledged.

At page 552 of *Parkinson v. Caldwell,* the court clearly holds:

> "Where the language is clear an agreement not to assign a debt is effective. The precise question was elaborately discussed by the New York Court of Appeals in Allhusen v. Caristo Const. Co., 303 N. Y. 446 (103 N. E. 2d 891), and at page 893 (103 N. E. 2d), the Court concluded 'in the light of the foregoing, we think it is reasonably clear that, while the Courts have striven to uphold freedom of assignability, they have not failed to recognize the concept

> of freedom to contract. In large measure they agree that, where appropriate language is used, assignments of money due under contracts may be prohibited.' "

At page 552 the California Court in the *Parkinson* case cites, with approval, 4 Corbin on Contracts, Section 572, page 486, as follows:

> "In any case, it is quite possible for the parties to show by apt words that rights created by the contract shall not be assignable. It is obvious that they mean exactly this and nothing else in case the contract is unilateral from the beginning. . . . So if A lends money to B, receiving from B a note that expressly declares that it is not assignable, there is no doubt that they mean A's right to the money to be nonassignable."

It is submitted that we have precisely the same situation existing in this case as is set forth in the above section of Corbin on Contracts and cited with approval by the California court in that each of the two Purchase Orders involved herein expressly declared that they were non-assignable.

In headnote 4 on pages 552 to 553 of the *Parkinson* case, the California court goes on to cite with approval Professor Williston's treatise on Contracts (Vol. 2, Sec. 422, p. 1214) which, among other things states:

> ". . . plaintiff's claimed rights arise out of the very contract embodying the provision now sought to be invalidated. The right to moneys under the contracts is but a companion to other jural relations forming an aggregation of actual and potential inter-related rights and obligations. No sound reason appears why an assignee should remain unaffected by a provision in the very contract which gave life to the claim he asserts."

The Court then goes on to state at page 553 that the California courts are in accord and cites *La Rue v. Groezinger,* 84 Cal. 281, and *Fairbanks v. Crump Irr. etc. Co., Inc.,* 108 Cal. App. 197 at p. 205, 291 Pac. 629, 292 Pac. 529.

At headnote 5 on page 553 of the *Parkinson* case, the Court answers an argument of unjust enrichment to the effect that more than the rights of the successor in interest to the assignor are involved, and cites California Civil Code, Section 3543 as applicable and embodying the following rules:

> "Where one of two innocent persons must suffer by the act of a third, he, by whose negligence it happened, must be the sufferer."

It is submitted that we have a very similar situation to the situation involved in the *Parkinson* case, in the instant proceeding. In the instant proceeding not only the rights of the assignor, Zipco, Inc., the bankrupt herein, and the rights of the Appellee, the assignee are involved, but also the rights of Fruehauf Trailer Co. and Com-Air Products, Inc., as well as the rights of all of the creditors of Zipco, Inc. which is now insolvent and bankrupt. It is clear that the Appellee accepted the assignment or assignments to it by Appellant's bankrupt, in direct violation of the language and prohibitions contained in the Purchase Orders. It is clear that the Appellee had but to read the contracts involved to ascertain that they specifically prohibited such assignments. It is also clear that the only moneys owing are owing by virtue of the Purchase Orders of the obligors, yet Aetna Factors Co., the Appellee, chose to claim under the very Purchase Orders yet to disregard the specific prohibitions contained therein. It is further submitted that this is exactly what

Parkinson v. Caldwell prohibits. It is further submitted that the creditors of the bankrupt corporation who are innocent third parties, including the taxing authorities, will be the persons who actually benefit if the Appellant prevails, rather than the Appellee benefiting by his own wrongful act and that in this situation the Appellant should prevail. In addition, it is clear from the record that a controversy exists between Fruehauf Trailer Co. and Com-Air Products, Inc., and the Appellee as to the amount owing, and that the obligors have refused to pay over to the Appellee the moneys involved and that under California State Law, if the Appellee should prevail in this proceeding, the obligors will merely refuse to pay the Appellee in this case and the net result will be that the Appellee will, in any event, not recover.

Conclusion.

The Memorandum Opinions of the Referee in Bankruptcy, *supra,* and the original Findings of Fact, Conclusions of Law and Order of the Referee, date December 23, 1957, and found at pages 35 to 43 of the Transcript of the Record, clearly followed the rule enunciated in *Parkinson v. Caldwell* and in *Allthusen v. Caristo Const. Co., supra,* to the effect that a prohibition against assignments contained in a contract renders an assignment made contrary to the said provisions, void. It has been amply demonstrated above, that these Findings and the Order based thereon were in accordance with existing California law which controlled the issue before the Court. It necessarily follows that the Order of the District Court reversing this Order and directing the Referee to prepare new Findings of Fact, Conclusions of Law and Order was erroneous and should be reversed on appeal. From this it follows that the subsequent Findings

of Fact, Conclusions of Law and Order of the Referee reversing himself, as directed by the District Court, are likewise erroneous and should be reversed on appeal.

For the reasons set forth above, it is respectfully urged that the Orders of the District Court appealed from in this consolidated appeal be reversed, and the original Findings of Fact, Conclusions of Law and Order of the Referee be affirmed.

Dated: February 12, 1959.

Respectfully submitted,

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